(10) (9)

Nos. 95-966, 95-977

In The

Supreme Court of the United States

October Term, 1995

KEVIN M. O'GILVIE and STEPHANIE L. O'GILVIE, minors,

Petitioners,

-and-

KELLY M. O'GILVIE,

Petitioner,

vs.

UNITED STATES OF AMERICA,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

SUPPLEMENTAL BRIEF FOR PETITIONERS KEVIN M. O'GILVIE AND STEPHANIE L. O'GILVIE, MINORS

ROBERT M. HUGHES
Counsel of Record
GREGORY L. FRANKEN
DAVID B. SUTTON
BEVER, DYE, MUSTARD & BELIN, L.C.
Attorneys for Petitioners Kevin M. O'Gilvie and Stephanie L. O'Gilvie, minors
106 West Douglas
Suite 700
Wichita, Kansas 67202
(316) 263-8294

STEPHEN R. McALLISTER
Of Counsel
University of Kansas School of Law
Green Hall
Lawrence, Kansas 66045
(913) 864-4550

8702-A
Lutz Appellate Services, Inc.
(800) 3 APPEAL • (800) 5 APPEAL • (800) BRIEF 21

16 PP

TABLE OF CONTENTS

TABLE OF CITATIONS

Cases Cited:

Statutes Cited:

Contents

THE ISSUES PRESENTED IN *O'GILVIE V. UNITED STATES* CONTINUE TO MERIT THE PLENARY REVIEW OF THIS COURT

This supplemental brief is filed pursuant to Rule 25.5 of the Rules of this Court and in response to the supplemental brief filed by the United States in this case. The United States filed a supplemental brief to bring to this Court's attention the enactment of the Small Business Job Protection Act of 1996, which *prospectively* alters § 104(a)(2) of the Internal Revenue Code, the statutory provision at issue in this case. The United States correctly concludes that the 1996 statutory amendments "do not resolve" the taxation question in this case, Supplemental Brief for the United States at 3, and admits that Congress explicitly stated in its conference report on the amendments that "'[n]o inference is intended' as to the proper interpretation of the statute prior to its amendment." *Id.* at n.1 (quoting H.R. Conf. Rep. No. 737, 104th Cong., 2d Sess. 301 (1996)). The petitioners in No. 95-966 (hereinafter the "O'Gilvie children") agree completely. Thus, Congress, the United States and the O'Gilvie children are in unanimous agreement that the 1996 statutory amendments have no bearing on the resolution of the O'Gilvie children's case, and Case No. 95-977 consolidated with it (hereinafter collectively referred to as the "present cases"), now before the Court.

That consensus notwithstanding, the United States ventures that the mere enactment of these prospective amendments may cause this Court "to consider dismissing the writs of certiorari in the present cases as improvidently granted." *Id.* at n.2. The only improvidence to be found is the United States' suggestion of dismissal at this late date. The unspecified implication of the United States' suggestion in footnote 2 is that the 1996 amendments to § 104(a)(2) render the present cases moot. They do not. The United States has admitted the 1996 amendments

"do not resolve" the exclusion of punitive damages issue for the present cases. *Id.* at 3. Therefore, the suggestion of dismissal by the United States logically contradicts its own previous conclusion regarding the amendments' effect (or lack thereof). As quoted in the United States' supplemental brief, Congress expressly intended "no inference" regarding the exclusion of punitive damages prior to the effective date of the Small Business Job Protection Act of 1996 — its date of enactment, August 20, 1996. This lack of an inference applies specifically to the resolution of the O'Gilvie children's case now before the Court, of which Congress took explicit notice in its conference report.[1] The split in the circuits which existed on the exclusion of punitive damages under § 104(a)(2) when the Court granted certiorari in March of this year continues to exist following the August 1996 amendments to § 104(a)(2). The amendments do not purport to, and do not, resolve that split. Any implication by the United States to the contrary is erroneous.

The United States' suggestion of dismissal is ill-made for several other reasons. First, the petitions for a writ of certiorari in the present cases fully informed the Court of the amendments to § 104(a)(2) in 1989 which significantly changed its operative language, but which do not apply to the present cases because they arose prior to the effective date of the 1989 amendments. *See, e.g.*, No. 95-966, Pet. for a Writ of Cert. 13-14. Nonetheless, the Court granted certiorari, thereby rejecting any notion that the exclusion of punitive damages question under the pre-1989 version of § 104(a)(2) — the issue common to both of the present cases before the Court — no longer merited the Court's attention. The United States offers no reason or rationale why the 1996

1. Joint Explanation of Conferees on HR 3448, Small Business Job Protection Act of 1996 at 141 n.54. *See* Appendix 1a-5a for complete text of Joint Explanation of Conferees on HR 3448, Small Business Job Protection Act of 1996, pertinent to amendments to Internal Revenue Code § 104(a)(2).

amendments now lead to a contrary conclusion or should suggest that the Court erred in its determination that these cases merit plenary review.

As noted in the petitioners' brief on the merits (Pet. Br. 31-32), Congress in 1989 amended § 104(a)(2) to provide that the exclusion thereunder "shall not apply to any punitive damages in connection with a case not involving physical injury or physical sickness." Omnibus Budget Reconciliation Act of 1989, Pub. L. No. 101-239, Section 7641, 103 Stat. 2106, 2379. In explaining the rationale of the 1989 amendment the House Ways and Means Committee stated that damages for personal injuries should only be excluded when physical personal injuries were involved. *See* Revenue Reconciliation Bill of 1989, Explanation of Revenue Provisions as approved by the House Ways and Means Committee on September 14, 1989, at 238. The Conference Committee agreed that "the exclusion for damages received for personal injury does not apply to punitive damages in cases not involving physical injury or sickness." Revenue Provisions of Conference Agreement on H.R. 3299, Omnibus Budget Reconciliation Act of 1989, at 147. While acknowledging that the 1989 amendment does not directly control the present cases by reason of its effective date, the petitioners have asserted (Pet. Br. 31) a reasonable conclusion to be made from the 1989 amendment is that prior to the amendment all punitive damages received on account of personal injuries were excluded from taxation, while after the 1989 amendment only punitive damages received in cases involving physical personal injuries were excluded. This Court has previously reached just such a conclusion. "Congress amended § 104(a) to allow the exclusion of *punitive* damages only in cases involving 'physical injury or physical sickness.' " *United States v. Burke*, 504 U.S. 229, 235 n.6 (1992) (emphasis in original).

Interestingly, the United States' response to this analysis of

the 1989 amendment was to declare that the 1989 amendment is "not at issue in the present case, which involves events that preceded the effective date of that amendment." U.S. Br. 29.[2] It is ironic that the United States now seeks to have the present cases irrevocably dismissed from plenary review by this Court on the basis of an even later amendment to § 104(a)(2), an amendment which the United States admits does not resolve the present cases. Contrary to the suggestion of the United States, the 1996 amendment is "not at issue in the present case, which involves events that preceded the effective date of that amendment."

Second, Cases No. 95-966 and No. 95-977 present additional issues on which the Court granted certiorari but which the United States does not mention in its supplemental brief. These additional issues are legally distinct from the taxation issue on which the United States focuses. Moreover, these issues may be independently determinative of the outcome of the present cases.

The O'Gilvie children have raised, and this Court has granted certiorari on, the issue of whether the triggering event which commences the two year statute of limitations under 26 U.S.C. § 6532(b), for a suit by the United States to recover a refund erroneously made, is the issuance or mailing of the refund check by the United States or its receipt by the taxpayer. For the reasons set forth at pages 34-41 of their brief on the merits and at pages 15-19 of their reply brief, the O'Gilvie children's case

2. The United States advanced the same argument in its brief in *Commissioner v. Schleier*, 515 U.S. __, 115 S. Ct. 2159 (1995), wherein the United States further noted its disagreement with this Court's analysis in *Burke* of the 1989 amendment. Brief for the United States, *Commissioner v. Schleier*, No. 94-500, at 33, n.22. The United States' unwillingness to accept this Court's interpretation of the 1989 amendment has perpetuated the uncertainty and confusion surrounding the scope of § 104(a)(2).

could be decided by the resolution of this issue without the Court ruling on the § 104(a)(2) exclusion issue. The United States' suggestion of dismissal at this late date would deprive the O'Gilvie children of the review, previously granted, on this possible basis for the Court's judgment. The same is equally true of the civil procedure question presented in No. 95-977 concerning whether the federal district court properly modified its judgment.

Third, the present cases remain worthy of the commitment of the judicial resources this Court allocated to them in originally granting certiorari. The petitioners are mindful that the "decision to grant certiorari represents a commitment of scarce judicial resources with a view to deciding the merits of one or more of the questions presented in the petition." *Oklahoma City v. Tuttle*, 471 U.S. 808, 816 (1985). The 1996 amendments to § 104(a)(2), by the United States' own admission, do not decide the merits of the present cases. The O'Gilvie children have at issue a tax liability, plus accrued interest thereon, totaling more than $1.39 million. Their father, Kelly O'Gilvie, the petitioner in No. 95-977, has a similar amount at issue. Cases involving amounts of this magnitude pertaining to an issue on which a split in the circuits exists properly warrant a commitment of the Court's scarce judicial resources, as the Court determined last March.

More importantly, beyond the significance of the present cases to the petitioners, this Court through them can resolve years of uncertainty and confusion regarding the scope of the § 104(a)(2) exclusion as to punitive damages received on account of physical injuries or sickness—an issue which the Court has never directly addressed. The significance of cases involving punitive damages awards, both in terms of the prevalence of such cases and the magnitude of the awards, has not escaped the notice of this Court. *See, e.g., Pacific Mutual Life Insurance Co. v. Haslip*, 499 U.S. 1, 8 n.4 (1990)

("[p]unitive damages are today awarded with a frequency and in amounts that are startling"); *Browning-Ferris Industries of Vermont, Inc. v. Kelco Disposal, Inc.*, 492 U.S. 257, 282 (1989) (O'Connor, J., concurring in part and dissenting in part) ("[a]wards of punitive damages are skyrocketing"). This prevalence and magnitude of punitive damages awards is further underscored by the projected federal budget impact of the 1996 amendments to § 104(a)(2). The Joint Committee on Taxation in its Estimated Budget Effects of the Conference Agreement Relating to the Revenue Provisions of H.R. 3448, The "Small Business Job Protection Act of 1996," projects the modification of § 104(a)(2) to result in $662 million of additional federal revenues from 1996 through 2006. *Id.* at 6. This projection, undoubtedly based on historical punitive damages awards, highlights the magnitude of existing punitive damages awards cases unresolved by the Small Business Job Protection Act of 1996. While the 1996 amendment may resolve the issue for physical injuries or sickness occurring on or after August 20, 1996,[3] by deciding the merits of the present cases this Court can finally resolve the issue for the untold hundreds, if not thousands, of prevailing plaintiffs, similarly situated to the O'Gilvie children, who received prior to August 20, 1996 punitive damages awards for physical injuries or sickness.

The uncertainty of the scope of § 104(a)(2) has arguably existed since the enactment of the Revenue Act of 1918. *See* Pet. Br. 15-19, Pet. Reply Br. 8-11. The vacillating rulings of the Internal Revenue Service through the years have not clarified the issue. *See* Pet. Br. 27-31. The 1989 amendment to § 104(a)(2) has been subject to varying interpretations (*see* Pet. Br. 31-34, U.S. Br. 28-32) which have confused, not resolved, the exclusion

3. The 1996 amendment does not apply to punitive damages amounts received under a written binding agreement, court decree, or mediation award in effect on (or issued on or before) September 13, 1995. Joint Explanation of Conferees on HR 3448, Small Business Job Protection Act of 1996, at 143.

from taxation issue now before the Court.[4] Deciding the present cases on the merits is a worthy use of the Court's resources in order to finally resolve the taxation issue in all the pending punitive damages cases which arose before August 20, 1996 and which are therefore unaddressed by the 1996 amendments.

Finally, at this time, the present cases have been fully briefed by all of the parties, and the Court has scheduled oral argument for October 9, 1996. The United States made the argument in its brief in opposition to the petitions for a writ of certiorari that these cases do not warrant plenary review and the Court rejected it. The United States' recent suggestion that the Court essentially erred in granting certiorari also should be rejected.[5] Judgment in the present cases should be on the merits as determined by this Court. Under the circumstances, any other method of terminating these cases would be inequitable to the petitioners who have expended substantial resources since the grant of certiorari in briefing their case to this Court and preparing for oral argument before it.

4. *See* note 2, *supra*.

5. *See* R. Stern, E. Gressman, S. Shapiro & K. Geller, Supreme Court Practice 231-33, 258-62 (7th ed. 1993).

CONCLUSION

For all of the foregoing reasons, the Court should decline the United States' suggestion to revisit, at this late date, the Court's original decision to grant plenary review of the several issues presented in Nos. 95-966 and 95-977.

Respectfully submitted,

ROBERT M. HUGHES
Counsel of Record
GREGORY L. FRANKEN
DAVID B. SUTTON
BEVER, DYE, MUSTARD
& BELIN, L.C.
Attorneys for Petitioners
Kevin M. O'Gilvie and
Stephanie L. O'Gilvie, Minors
106 West Douglas, Suite 700
Wichita, Kansas 67202
(316) 263-8294

STEPHEN R. McALLISTER
Of Counsel
UNIVERSITY OF KANSAS
SCHOOL OF LAW
Green Hall
Lawrence, Kansas 66045
(913) 864-4550

APPENDIX

Joint Explanation of Conferees on HR 3448, Small Business Job Protection Act of 1996

Revenue Provisions (Title I)

* * *

VI. Revenue Offsets

* * *

5. Modify exclusion of damages received on account of personal injury or sickness (sec. 1605 of the House bill and sec. 1603 of the Senate amendment)

Present Law

Under present law, gross income does not include any damages received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal injury or sickness (sec. 104(a)(2)).

The exclusion from gross income of damages received on account of personal injury or sickness specifically does not apply to punitive damages received in connection with a case not involving physical injury or sickness. Courts presently differ as to whether the exclusion applies to punitive damages received in connection with a case involving a physical injury or physical sickness.[54] Certain States provide that, in the case of claims

54. The Supreme Court recently agreed to decide whether punitive damages awarded in a physical injury lawsuit are excludable from gross income. *O'gilvie v. U.S.*, 66 F.3d 1550 (10th Cir. 1995), *cert. granted*, 64 (Cont'd)

under a wrongful death statute, only punitive damages may be awarded.

Courts have interpreted the exclusion from gross income of damages received on account of personal injury or sickness broadly in some cases to cover awards for personal injury that do not relate to a physical injury or sickness. For example, some courts have held that the exclusion applies to damages in cases involving certain forms of employment discrimination and injury to reputation where there is no physical injury or sickness. The damages received in these cases general consist of back pay and other awards intended to compensate the claimant for lost wages or lost profits. The Supreme Court recently held that damages received based on a claim under the Age Discrimination in Employment Act could not be excluded from income.[55] In light of the Supreme Court decision, the Internal Revenue Service has suspended existing guidance on the tax treatment of damages received on account of other forms of employment discrimination.

(Cont'd)

U.S.L.W. 3639 (U.S. March 25, 1996) (No. 95-966). Also, the Tax Court recently held that if punitive damages are not of a compensatory nature, they are not excludable from income, regardless of whether the underlying claim involved a physical injury or physical sickness. *Bagley v. Commissioner*, 105 T.C. No. 27 (1995).

55. *Schleier v. Commissioner*, 115 S. Ct. 2159 (1995).

House Bill

Include in income all punitive damages

The House bill provides that the exclusion from gross income does not apply to any punitive damages received on account of personal injury or sickness whether or not related to a physical injury or physical sickness. Under the House bill, present law continues to apply to punitive damages received in a wrongful death action if the applicable State law (as in effect on September 13, 1995 without regard to subsequent modification) provides, or has been construed to provide by a court decision issued on or before such date, that only punitive damages may be awarded in a wrongful death action. No inference is intended as to the application of the exclusion to punitive damages prior to the effective date of the House bill in connection with a case involving a physical injury or physical sickness.

Include in income damage recoveries for nonphysical injuries

The House bill provides that the exclusion from gross income only applies to damages received on account of a personal physical injury or physical sickness. If an action has its origin in a physical injury or physical sickness, then all damages (other than punitive damages) that flow therefrom are treated as payments received on account of physical injury or physical sickness whether or not the recipient of the damages is the injured party. For example, damages (other than punitive damages) received by an individual on account of a claim for loss of consortium due to the physical injury or physical sickness of such individual's spouse are excludable from gross income. In addition, damages (other than punitive damages) received on account of a claim of wrongful death continue to be excludable from taxable income as under present law.

The House bill also specifically provides that emotional distress is not considered a physical injury or physical sickness.[56] Thus, the exclusion from gross income does not apply to any damages received (other than for medical expenses as discussed below) based on a claim of employment discrimination or injury to reputation accompanied by a claim of emotional distress. Because all damages received on account of physical injury or physical sickness are excludable from gross income, the exclusion from gross income applies to any damages received based on a claim of emotional distress that is attributable to a physical injury or physical sickness. In addition, the exclusion from gross income specifically applies to the amount of damages received that is not in excess of the amount paid for medical care attributable to emotional distress.

No inference is intended as to the application of the exclusion to damages prior to the effective date of the House bill in connection with a case not involving a physical injury or physical sickness.

Effective date. — The provisions generally are effective with respect to amounts received after June 30, 1996. The provisions do not apply to amounts received under a written binding agreement, court decree, or mediation award on (or issued on or before) September 13, 1995.

---

56. It is intended that the term emotional distress includes physical symptoms (e.g., insomnia, headaches, stomach disorders) which may result from such emotional distress.

Senate Amendment

Include in income all punitive damages

The Senate amendment is the same as the House bill.

Include in income damage recoveries for nonphysical injuries

No provision.

Conference Agreement

Include in income all punitive damages

The conference agreement follows the House bill and the Senate amendment.

Include in income damage recoveries for nonphysical injuries

The conference agreement follows the House bill.

Effective date — The provisions generally are effective with respect to amounts received after date of enactment. The provisions do not apply to amounts received under a written binding agreement, court decree, or mediation award in effect on (or issued on or before) September 13, 1995.